No. 83-1782

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

THOMAS R. ALLEN, JR.,
Petitioner,

v.

PENSION BENEFIT GUARANTY CORPORATION,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF FOR RESPONDENT PENSION BENEFIT GUARANTY CORPORATION IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether a claim by the PBGC against trustees for the recovery of pension plan funds lost through (1) self-dealing and breaches of fiduciary duties under Pennsylvania law prior to 1975 and (2) failure to take corrective action after January 1, 1975 is barred by the provision of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1144, which makes ERISA inapplicable to "any act or omission which occurred before January 1, 1975."

2. Whether a trustee may avoid liability for failure to secure tenuous loans of a pension plan by claiming that efforts to secure such loans would have been "meaningless" in light of the insolvency of the debtors.

3. Whether a fiduciary is civilly liable under ERISA even if he did not "willfully" waste the assets of the pension plan.

PARTIES TO THE PROCEEDING

The Pension Benefit Guaranty Corporation ("PBGC") is a United States government agency created by 29 U.S.C. § 1302(a). Thomas R. Allen, Jr., is a resident of Pennsylvania. Co-defendants in the district court were Morton J. Greene, a resident of Pennsylvania, and Economy Industrial Properties, a Pennsylvania partnership in which Messrs. Allen and Greene are general partners.

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OPINIONS BELOW

The judgment of the court of appeals (Pet. App. C) is reported at 727 F.2d 1100. The opinion of the district court (Pet. App. A) is reported at 570 F. Supp. 1483.

JURISDICTION

The judgment of the court of appeals was entered on January 10, 1984. A petition for a writ of certiorari was filed on April 9, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The relevant sections of ERISA (29 U.S.C. §§ 1001, 1105, 1144) appear at Pet. App. D-1 through D-9.

STATEMENT

This litigation involves the liability of two fiduciaries of four defined benefit pension plans under Pennsylvania state law and the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001-1381 ("ERISA").[1] The stipulated facts—which were reproduced as an exhibit to the opinion of the district court (570 F. Supp. at 1505-1509)—show that petitioner participated with his co-trustee in a course of self-dealing and imprudent conduct involving the misappropriation of nearly all the assets of the pension plans for the benefit of the companies in which the trustees held interests as directors, officers, or shareholders. The trustees' course of conduct involved four components: (1) self-dealing and imprudent loans between 1970 and 1974, before ERISA was enacted; (2) failure to collect or secure the loans both before and after ERISA's enactment; (3) failure to collect from their companies contributions for the plans both before and after ERISA's enactment; and (4) a post-ERISA sale and lease-back transaction with their own partnership, intended, according to the district court, "to transfer money from the plans to the financially ailing businesses" and "to further [the trustees'] own financial interests, and the interests of their partnership, at the expense of the plans." Pet. App. A-65; 570 F. Supp. 1501.

Although petitioner's co-trustee, Morton J. Greene, was characterized by the district court as "the primary violator" because Greene signed the withdrawal and deposit

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[1] ERISA was amended in 1980 by the Multiemployer Pension Plan Amendments Act of 1980, 94 Stat. 1208-1311 (1980). The 1980 amendments to ERISA do not apply to this case. Accordingly, citations to ERISA will be to the 1974 statute as codified in the 1976 edition of the United States Code.

slips, petitioner signed a check for a large amount from a plan to one of the companies, and signed all unsecured demand notes for the loans. Pet. App. A-35-A-36; 570 F. Supp. 1494. The district court also found that petitioner "knew that the companies were not meeting their financial obligations and, specifically, that contributions were being withheld from the employees, but not paid to the funds." Pet. App. A-47; 570 F. Supp. 1497. And while Greene signed the post-ERISA lease with the trustees' partnership on behalf of three of the plans, petitioner also signed on behalf of the partnership. Pet. App. A-62; 570 F. Supp. 1500.

Neither trustee made any effort to collect the loans or the contributions, or to obtain demand notes or judgments. Neither made any effort to diversify the plans' investments. Pet. App. A-57; 570 F. Supp. 1499. Nor did the trustees notify the pensioners of the delinquent contributions. The district court also found that both trustees took part in "wash transactions" to conceal the shortages and "to make the records show loan transacitons rather than delinquent contributions." Pet. App. A-46; 570 F. Supp. 1496.

The district court rejected the claim that the trustees had resigned their positions through resignation letters purportedly written on the day before ERISA became law. The court found that no one else took over their duties, that the financial institutions that handled the trust accounts were not informed, and that the trustees actually did nothing more than "notif[y] themselves that they were resigning." Pet. App. A-50; 570 F. Supp. at 1497.

In May 1980, the PBGC, as statutory trustee, commenced a civil action in the United States District Court for the Western District of Pennsylvania against petitioner, Greene and their partnership to recover losses suffered by the four pension plans during the pre-ERISA and ERISA periods. The PBGC's amended complaint in-

voked jurisdiction under ERISA and asserted pendent jurisdiction over claims made under Pennsylvania law. Pet. App. A-87; 570 F. Supp. 1489, n.11.

Following discovery, the district court ruled on cross-motions for summary judgment. The PBGC's motion was granted, and a money judgment for $352,517.82, including pre-judgment interest, was entered. The district court held that petitioner and his co-defendant had breached their fiduciary duties under Pennsylvania law by making imprudent, unsecured and undiversified loans to their own companies, by engaging in self-dealing in making the loans, by failing to collect the employer contributions and to pay to the pension plans the withheld employee contributions, and by promoting their own interests at the expense of the interests of the beneficiaries of their trust.

The court also found that the trustees violated ERISA after it was enacted by failing to take proper corrective measures and by breaching their continuing duties to review and liquidate improvident investments. The court reasoned that petitioners made no attempt to obtain security for the unsecured demand notes, no attempt to secure judgment notes, no attempt to diversify assets, and no attempt to notify the pensioners of the delinquent contributions. Pet. App. A-52-A-60; 570 F. Supp. 1498-1500. The court also held that the post-ERISA lease between the plans and the trustees' partnership violated ERISA's "prohibited transactions" rules against leases between a plan and a party in interest, and awarded approximately $3,500 to the PBGC in rent improperly paid pursuant to the lease. On January 9, 1984, the court of appeals heard argument, and it affirmed the district court's judgment by summary order on the following day.

ARGUMENT

This is an egregious case of improper conduct by two trustees who looted several pension plans to provide funds for their own private businesses, which ultimately went bankrupt. The PBGC's successful claims against the petitioner are based on *both* Pennsylvania state law, which imposed liability for such conduct prior to the enactment of the federal statute, and ERISA. The district court concluded that federal jurisdiction was validly invoked under ERISA for the trustees' improper acts and omissions after January 1, 1975, when ERISA took effect, and that it had pendent jurisdiction to decide issues of liability under Pennsylvania law relating to the pre-1975 period. These conclusions were patently correct, were properly affirmed summarily by the court of appeals, present no issue of general importance, raise no conflict with decisions in any other Circuit, and do not warrant any further consideration.

1. Petitioner does not challenge the district court's reasoned conclusion that it had pendent jurisdiction over pre-ERISA claims made under Pennsylvania law governing fiduciary responsibility. *See* Pet. App. A-9-A-14; 570 F. Supp. 1488-1489. Nor does petitioner appear to challenge the district court's finding that he violated his fiduciary duties under State law, and that he would be liable, on these principles, for pre-ERISA acts.

This is not, in other words, a case in which substantive liability for acts committed before January 1, 1975, depends entirely on a provision of ERISA. Hence petitioner's assertion that the district court found him liable under ERISA only because he failed "to take corrective action after January 1, 1975" (Pet. 15) is simply erroneous. Petitioner was found liable under Pennsylvania law for the pre-ERISA period because he committed acts prior to January 1, 1975, which violated State law.

In considering whether federal jurisdiction existed,[2] the district court also held that a pension-plan trustee has a continuing duty under federal law to take proper measures after January 1, 1975, to reduce injury attributable to his pre-ERISA violations. The failure to do so constitutes a fiduciary violation under ERISA. As the Second Circuit observed in *Morrisey* v. *Curran*, 567 F.2d 546, 548-49 (2d Cir. 1977): "We have no doubt that under the 'prudent man' rule, which is codified in ERISA, the trustees here had a duty within a reasonable time after ERISA took effect to dispose of any part of the trust estate which would be improper to keep." In his concurring opinion in *Morrisey*, Judge Lumbard noted that the continuing breach concept also includes a duty to take "corrective action if there is a reasonable basis for the recovery of wasted assets from the receiver thereof, or of misused funds from the person who profited from the misuse." 567 F.2d at 550. This is a plainly correct proposition governing fiduciary duties under federal law, and petitioner has cited no contrary authority.

2. There is no substance to petitioner's contention that the insolvency of the trustees' companies rendered it "meaningless" to attempt to recover misspent funds after ERISA became law (Pet. 23-27). The district court rejected this curious claim, which would give greater leeway to trustees if they misdirected the funds of a pension plan to a hopelessly insolvent beneficiary rather than to one which has a chance of recovery. Moreover, the fact that the corporations were insolvent did not necessarily mean that there was no step that could reasonably have been taken to attempt to secure the "loans" that had previously been made. Indeed, if the corporations had

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[2] The court said that it had to decide whether ERISA applied "because of the jurisdictional question which it raises." Pet. App. A-11; 570 F. Supp. at 1488. After concluding that ERISA did apply, the court said that in view of that finding, "the Court can assume pendent jurisdiction over plaintiff's pre-ERISA, state law claims." Pet. App. A-14, 570 F. Supp. at 1489.

been controlled by third parties with whom the trustees dealt at arms' length, they might well have devised protective measures involving the individual assets of the principals who owned the corporations. In the present circumstances, where the corporations were controlled by the trustees themselves, they had no incentive to secure or otherwise protect the loans that the pension plans had made or the contributions that were due.

In any event, this issue turns largely on an appraisal of the facts, including the solvency of the corporate "borrowers." It is plainly not an issue deserving this Court's attention.

3. Petitioner's final contention is that after his purported resignation of December 31, 1974, he thought himself to be powerless and was, therefore, not guilty of any "willful" abuse of fiduciary obligations (Pet. 28-30). Petitioner does not, however, contest the district court's finding that he was aware of, and personally participated in, the conduct of his co-trustee prior to December 31, 1974. The district court ruled that under ERISA, a trustee has a continuing fiduciary status "absent a clear resignation, and a resignation is valid only when he has made adequate provision for continued prudent management of the plan assets." *See* Pet. App. A-51; 570 F. Supp. 1497, citing *Freund* v. *Marshall & Ilsley Bank*, 485 F. Supp. 629, 635 (W.D. Wis. 1979). Petitioner plainly did not meet that standard. Further, 29 U.S.C. § 1105(a)(3) makes a fiduciary liable on the basis of knowledge alone, "unless he makes reasonable efforts under the circumstances to remedy the breach." The record contains no evidence of any effort whatever by the petitioner "to remedy the breach."

Indeed, in February 1976, petitioner participated personally, on behalf of the trustees' partnership, in the lease agreement with the plans which continued the effort to use the plans to bail the trustees' corporations out of their financial problems. This transaction alone refutes

petitioner's claim that "his involvement with the trusts completely stopped" after the end of 1974 (Pet. 30). Even if he did not nominally act then on behalf of the pension plans, his actions amounted to a continuation of the earlier abuse of the trustees' authority.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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